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Supreme Court, U.S.
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No. 93-1080

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1993

Doctor's Associates, Inc.,

Petitioner,

v.

Dick DeWayne Cox, Jr. and
Substantial Enterprises, Inc.,

Respondents.

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE APPELLATE COURT OF ILLINOIS, FIFTH DISTRICT

BRIEF IN OPPOSITION

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QUESTIONS PRESENTED FOR REVIEW

I. Does a jury award of $1,000,000 in punitive damages violate the due process clause of the Fourteenth Amendment when the jury awarded $200,000 actual damages for breach of contract and $1,000,000 in punitive damages for the independent tort of intentional, fraudulent misrepresentation of fact which was also a cause of the breach of contract damages?

II. Does the award of punitive damages violate the due process clause of the Fourteenth Amendment when, as Petitioner concedes, Illinois has adequate procedural safeguards against excessive punitive damage awards, and Petitioner abandoned all claims for relief, under those adequate procedural safeguards, in its appeal to the Appellate Court of Illinois?

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STATEMENT OF THE CASE

Respondents correct and supplement the statement of the case submitted by petitioner, as follows:

In the question presented for review, and at Page 9 of the petition,

petitioner alleges "the jury awarded Substantial zero actual damages for Count II, but $1,000,000 in punitive damages".

That statement is inaccurate.

The jury was instructed it could award actual damages in Count I for breach of contract and punitive damages only, in Count II, if the jury found that petitioner was guilty of willful and wanton fraudulent misrepresentation of material facts in inducing respondents into the franchise agreements and in thereafter breaching the franchise agreements and if "as a direct consequence of the falsity of the defendant's representations, plaintiff was caused to suffer damages for breach of contract." See Page 50a of the Appendix to the petition for the quoted material.

The verdict submitted to the jury on

Count I is set forth below:

" VERDICT FORM A-1

We, the Jury, find for Plaintiff Substantial Enterprises, Inc. and against Defendant Doctor's Associates, Inc. on Count I of Plaintiff's Complaint. We assess damages in the sum of $_____."

The verdict form submitted to the jury on Count II provides:

" VERDICT FORM A-2

We, the Jury, find for Plaintiff Substantial Enterprises, Inc. and against Defendant Doctor's Associates, Inc. on Count II of Plaintiff's Complaint. We assess punitive damages in the sum of $_____."

Similar verdict forms were given to the jury permitting them to find against Plaintiff on Counts I and II.

The jury completed the verdict form by filling in $200,000 in actual damages

in the space provided in Verdict Form A-1 and $1,000,000 in punitive damages in the space provided in Verdict Form A-2.

The jury was not given the option of awarding actual damages under Count II. Counts I and II, in combination, submitted Plaintiff's claims for actual and punitive damages.

Petitioner's suggestion that the jury awarded zero actual damages and $1,000,000 punitive damages is simply inaccurate, or, as the very least misleading.

In the appeal to the Illinois Court of Appeals, Fifth District, petitioner did not raise any objections to the jury instructions. Petitioner did not claim the jury instructions were improper as to form. Petitioner did not claim the jury instructions were not supported by the

evidence.

After the verdict, petitioner moved the trial court for relief under 735 ILCS 5/2-1207 which provides:

> **5/2-1207. Punitive damages**
>
> "§ 2-1207. Punitive damages. The trial court may, in its discretion, with respect to punitive damages, determine whether a jury award for punitive damages is excessive, and if so, enter a remittitur and a conditional new trial.
>
> The trial court may also in its discretion, apportion the punitive damage award among the plaintiff, the plaintiff's attorney and the State of Illinois Department of Rehabilitation Services. The amount of the award paid from the punitive damages to the plaintiff's attorney shall be reasonable and without regard to any contingent fee contract, except that such amount

> shall not exceed the amount authorized by the contingent fee contract. In apportioning punitive damages as provided in this Section, the court shall consider, among other factors it deems relevant, whether any special duty was owed by the defendant to the plaintiff."

The trial court denied petitioner's request for relief under 735 ILCS 5/2-1207.

Petitioner then abandoned its claim for relief under 735 ILCS 5/2-1207 in the Court of Appeals, by failing to raise that issue at the appellate court level.

Petitioner required each franchisee to enter into a sublease with a sub-leasing company. The subleasing company in this case was Subway Sandwich Shops, Inc. Subway Sandwich Shops, Inc. was an alter ego and/or agent of petitioner which operated exclusively under the

control and at the direction of petitioner. Each sublease provided that a default, by the franchisee, of the franchise agreement was a breach of the sublease and grounds for eviction.

While petitioner represented that all disputes under the franchise agreement would be resolved by arbitration, in fact, it used its alter ego subleasing companies to file eviction lawsuits against the franchisees, to resolve petitioner's claims against the franchisees, under the franchise agreement, while requiring the franchisees to arbitrate their claims, arising out of the same disputes, in Connecticut.

Petitioner represented that its business methods were democratic and anti-authoritarian. In fact it used the

sublease arrangement and the threat of eviction to totally control and dominate its franchisees. Using the threat of eviction, petitioner could require any franchisee to risk losing its entire investment in order to resolve any dispute with petitioner.

Respondents had purchased eight franchise agreements and were operating five franchise stores. Respondents had the approval of petitioner to open a large number of stores in the St. Louis area. At the time the market for Subway stores in the St. Louis metropolitan area was wide open. There were very few Subway stores in the area.

Petitioner also represented that it would not unreasonably withhold approval of cite locations for Subway stores.

Respondents obtained the approval of

petitioner to open three Subway stores in May Company shopping malls in the St. Louis, Missouri metropolitan area (which includes the Illinois counties of St. Clair and Madison). After obtaining approval from petitioner, respondents entered into lease agreements for two of these locations with the May Company. Petitioner then reneged on its prior approval of these locations and refused to permit respondents to go forward. Faced with threats of breach of lease by the May Company, respondents opened deli stores in the two locations under lease under the name of "Sub-City".

Thereafter, respondents offered to convert these Sub-City stores to Subway stores and open them under the three franchise agreements which had already been purchased, but, under which no

stores had yet been opened. Petitioner refused.

After respondents had opened the first Sub-City store, expending more than $50,000 in leasehold improvements, petitioner agreed to permit respondents to convert the store to a Subway store, but required respondents to do this at their cost, required respondents to purchase the existing Subway store of another franchisee (whose store was near the mall but was in a separate market, as shopping center malls are considered to be a separate market from the surrounding area) and required respondents to pay royalties and other fees on past sales at the Sub-City store.

The net effect of these requirements would have cost respondents more than $75,000 for correcting a problem that was

created when petitioner reneged on its prior approval of the three mall locations.

Respondents refused to make these changes at their costs, but were willing to discuss possible compromises by both parties.

Notwithstanding its representations to the contrary, petitioner refused to discuss any compromise and refused to change its position, threatening respondents with eviction and bankruptcy. Thereafter petitioner reneged on its prior written approval for a Subway store location in Granite City, Illinois. Respondents had requested this location pursuant to one of their purchased franchises, for which a Subway store had not yet been opened.

Petitioner also advised respondents

they were stopped cold on their previously approved plan to open as many stores as possible in the St. Louis metropolitan area.

Thereafter petitioner attempted to employ its standard procedure of requiring respondents to arbitrate their claims against it in Connecticut while it litigated its claims, arising out of the same dispute, against respondents in the form of eviction lawsuits filed in the name of its alter ego subleasing company, Subway Sandwich Shops, Inc.

Petitioner is a sub-chapter S corporation, which means all corporate income is taxed to the shareholders. Frederick DeLuca and Peter Buck are the two equal (50% each) shareholders of petitioner. Petitioner had a net worth of $7,000,000. Petitioner was able to

generate taxable income for its two share-holders in the total sum of $10,000,000 in 1987, $20,000,000 in 1988, $32,000,000 in 1989 and $54,000,000 in 1990, totaling $116,000,000 (divided equally between Mr. DeLuca and Mr. Buck) for this four-year period. See the Appellate Court opinion set forth at Pages 24a and 25a of the Appendix to the petition.

At the time of trial, petitioner had franchise agreements for more than 6,000 franchise stores throughout the United States.

SUMMARY OF THE ARGUMENT

I.

The jury award of $1,000,000 in punitive damages for willful and wanton, intentional, fraudulent misrepresen-

tations of material fact, where such false misrepresentations contributed to cause a breach of contract, which resulted in actual damages of $200,000, does not violate the due process clause of the Fourteenth Amendment, and such damages are not constitutionally excessive where petitioner engages in the same pattern of misconduct with respect to all of its 6,000 franchise stores, and where petitioner earned taxable income of $116,000,000, on a net worth of $7,000,000, during the four years preceding the jury award.

II.

The award of punitive damages does not violate the due process clause of the Fourteenth Amendment when, as conceded by petitioner at Page 11 of its petition,

there is no claim that the Illinois procedural safeguards against excessive punitive damages are so lacking that all punitive damage awards in Illinois violate the due process clause, and where petitioner initially sought relief under the Illinois statutory procedural safeguards, then abandoned that claim for relief, under said, admittedly adequate, safeguards at the appellate level.

ARGUMENT

I.

The award of $1,000,000 in punitive damages was for willful and wanton, intentional, fraudulent misrepresentations of material fact. The jury was instructed they could award punitive damages for this conduct if, among other things, "as a direct consequence of the

falsity of the defendant's representations, plaintiff was caused to suffer damages for breach of contract." See that portion of one of the jury instructions cited at Page 50a of the Appendix to the petition.

The jury was clearly instructed that their award of punitive damages for intentional fraudulent conduct related to their award of actual damages for breach of contract.

The jury instructions and the verdict form permitted the jury to award only actual damages under Count I and permitted the jury to award only punitive damages under Count II.

Petitioners contention that the jury awarded "zero actual damages for Count II, but $1,000,000 in punitive damages" is simply a misstatement of fact. See

the top of Page 9 of the petition.

Petitioner argues "a party should not be financially punished for conduct that causes no injury." Also see the petition at the top of Page 9.

The evidence, the jury instructions, and the verdict clearly establish that respondents suffered significant injury and damage.

Petitioner has developed a franchise system which generates an incredible amount of money considering petitioner's investment. On a net worth of $7,000,000, petitioner generated $54,000,000 in taxable income in 1990. The pattern established from 1987 through 1990 indicates the taxable income is increasing exponentially.

Under the franchise system employed, the franchisees provide the capital, do

the work and take the financial risk of success. Petitioner provides the know how, the trade name and, in exchange, receives an initial franchise fee and 10 1/2% of the gross sales of each franchisee (8% for royalty and 2 1/2% for an advertising fee).

In order to keep generating income at these levels, petitioner believes it is important to keep each franchisee under its total domination and control. The sublease eviction procedure is one method employed by petitioner to exert control over the franchisees. Any franchisee who dares to complain must be made into an example, for the benefit of the other franchisees.

Petitioner exerted its control over the respondents in this case by refusing to permit the respondents to open Subway

stores for three franchise agreements they had purchased, by reneging on the location in Granite City which had previously been approved, by refusing to sell respondents any additional franchises pursuant to a prior agreement to permit them to open as many stores as possible and by requiring respondents to pay the cost of converting the Sub-City store to a Subway store when that expense was incurred because petitioner first approved locations in the three malls, then reneged after respondents had made commitments to the May Company to lease locations in two of the malls.

Petitioner also attempted to use its standard tactic of requiring respondents to arbitrate in Connecticut while filing eviction lawsuits against the respondents to resolve petitioner's claims against

the respondents arising out of the same dispute. In this case petitioner was unsuccessful. The trial court ruled petitioner waived its right to arbitrate by filing eviction lawsuits in the name of its alter ego and/or agent Subway Sandwich Shops, Inc. Petitioner appealed and the appellate court affirmed. See *Yates v. Doctor's Associates*, 193 Ill. App. 3d 431, 140 Ill. Dec. 359, 549 N.E.2d 1010 (Ill. App. 1990). The appellate court held that the act of Subway Sandwich Shops, Inc. in filing the eviction lawsuits was the act of petitioner, because Subway Sandwich Shops, Inc. was either the alter ego and/or agent of the petitioner. See *Yates v. Doctor's Associates, Inc.*, 549 N.E.2d 1010 at 1016 and 1017.

The $1,000,000 punitive damage award

is only five times as great as the actual damage award. In *TXO Production Corp. v. Alliance Resources Corp.*, 113 S.Ct. 2711, ____ U. S.____ (1993) the punitive damage award was approximately 520 times greater than the actual damage award.

In the case at bar, there is evidence that petitioner's oppressive and fraudulent behavior is widespread. It uses alter ego corporations to file eviction lawsuits for the purpose of controlling the franchisees while representing to the franchisees that all disputes under the franchise agreement will be arbitrated and while representing that its business methods are anti-authoritarian and democratic. It earns huge sums, compared to its net worth, by operating in this fashion.

Petitioner has not raised any issue

which was not previously addressed by this court in *TXO Production Corp. v. Alliance Resources Corp.*, 113 S.Ct. 2711, ____ U.S. ____ (1993), *Pacific Mutual Life Ins. Co. v. Haslip*, 499 U.S. 1, 111 S.Ct. 1032, 113 L.Ed. 2d 1 (1991) and *Bankers Life & Cas. Co. v. Crenshaw*, 486 U.S. 71, 108 S.Ct. 1645, 100 L.Ed. 2d 62 (1988).

II.

Petitioner concedes that Illinois procedural safeguard against excessive punitive damage awards are adequate and do not violate the due process clause. See the petition at the bottom of Page 11. Petitioner states that its point "is that the procedural safeguards in Illinois utterly failed in this case." See the petition at the bottom of Page 11.

735 ILCS 5/2-1207 permits the trial court to determine whether a jury award for punitive damages is excessive, and, if so, to enter a remittitur and a conditional new trial.

The trial court also has discretion to apportion any punitive damage award among the plaintiff, the plaintiff's attorney and the State of Illinois Department of Rehabilitation Services.

Petitioner sought relief under 735 ILCS 5/2-1207 at the trial court level. The trial court denied petitioner's request for relief under this statute. Petitioner then abandoned this issue on appeal.

Having abandoned state court review under the Illinois statutory procedural safeguard against excessive punitive damage awards, petitioner may not now

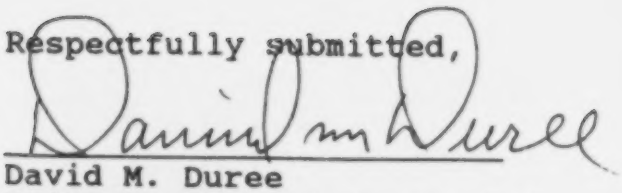
claim a due process violation in this court on the grounds that "the procedural safeguards in Illinois utterly failed in this case."

It is elementary that petitioner may not claim the Illinois procedural safeguards are constitutionally defective when petitioner abandoned, on appeal, its claim for relief under those procedural safeguards.

CONCLUSION

For the foregoing reasons, respondents respectfully submit that the petition for a writ of certiorari should be denied.

Respectfully submitted,



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